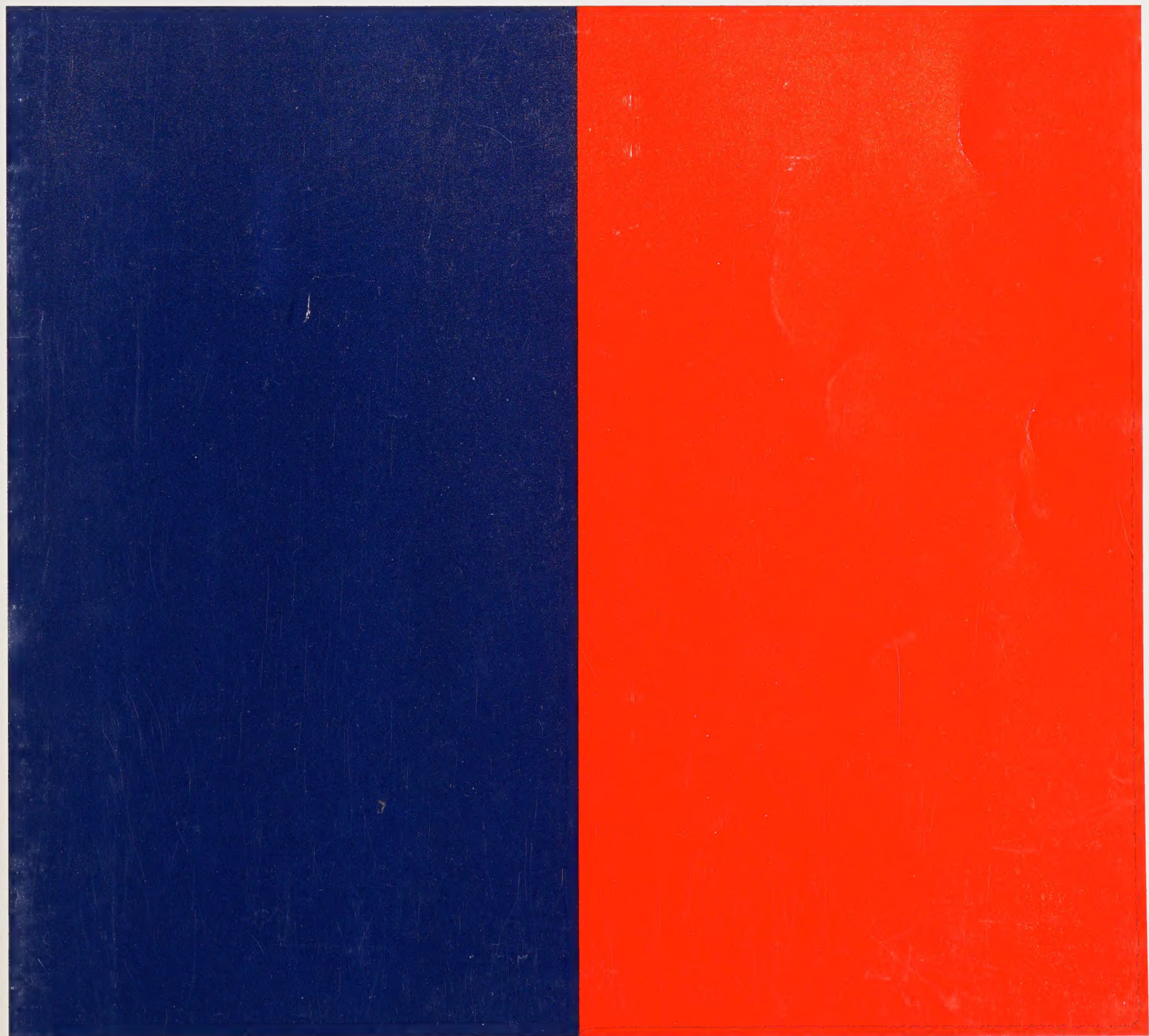


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Mr Scott



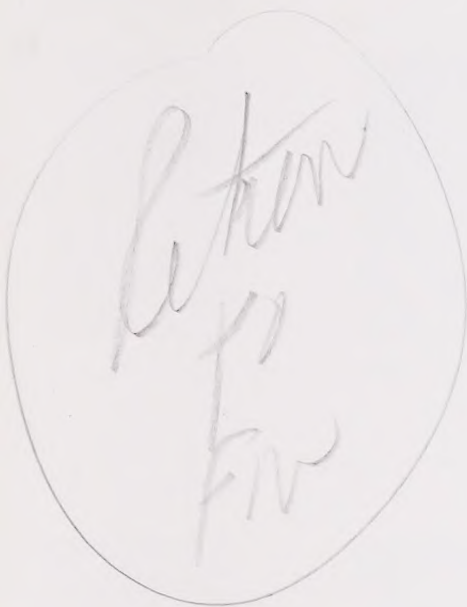
Lee



Rothmans

THE GREATEST NAME
IN CIGARETTES





ROTHMANS OF PALL MALL CANADA LIMITED
ANNUAL REPORT 1967

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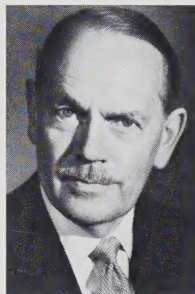
Directors:



JOEL W. ALDRED, TORONTO
PRESIDENT
JOEL W. ALDRED LTD.



CHARLES F. W. BURNS, KING, ONT.
CHAIRMAN
BURNS BROS. AND DENTON LIMITED



SIR FRANCIS DE GUINGAND,
K.B.E., C.B., D.S.O.
JOHANNESBURG
DIRECTOR
ROTHMANS GROUP COMPANIES



JOHN H. DEVLIN, TORONTO
PRESIDENT
ROTHMANS OF PALL MALL
CANADA LIMITED



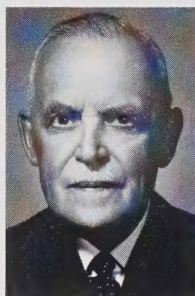
SHIRLEY G. DIXON, O.B.E., Q.C.,
MONTREAL
FORMERLY VICE PRESIDENT
AND DIRECTOR
THE ROYAL TRUST COMPANY



HAROLD S. FOLEY, VANCOUVER
PRESIDENT
SCANLON HOLDINGS LIMITED



CHARLES A. MASSEY, TORONTO
FORMERLY PRESIDENT AND DIRECTOR
LEVER BROTHERS LIMITED



RT. HON. LOUIS S. ST-LAURENT,
Q.C., LL.D., P.C.
QUEBEC, P.Q.
PARTNER—ST-LAURENT, MONAST,
DESMEULES & WALTERS



JOHN E. SHAFFNER,
PORT WILLIAMS, N.S.
PRESIDENT AND DIRECTOR
M. W. GRAVES & CO. LTD.



WILMAT TENNYSON, TORONTO
VICE PRESIDENT MARKETING
ROTHMANS OF PALL MALL
CANADA LIMITED

Officers:

Chairman of the Board
President
Vice President Marketing
Treasurer
Secretary

THE RIGHT HONOURABLE LOUIS STEPHEN ST-LAURENT, Q.C., LL.D., P.C.

JOHN HERBERT DEVLIN

WILMAT TENNYSON

PAUL JACOBUS ERASMUS

ROBERT HOWIE HAWKES

Head Office:

75 DUFFLAW ROAD, TORONTO 19, ONTARIO

Auditors:

PRICE WATERHOUSE & CO.

Bank:

BANK OF MONTREAL

Registrar & Transfer Agent:

THE ROYAL TRUST COMPANY

Solicitors:

WAHN, MAYER, SMITH, CREBER, LYONS, TORRANCE & STEVENSON

Directors' Report

Sales and earnings for the year ended June 30, 1967, were the highest in the history of the Company. This is the fifth consecutive year that new records have been set for sales and earnings.

During the past year sales increased by \$18,938,000 or 13 percent, and net earnings increased by \$597,000 or a 19 percent gain over the previous year. Earnings per share increased from \$2.44 to \$2.89.

As mentioned in last year's annual report, your Company established two additional "firsts" in the Canadian cigarette market with the introduction of Dunhill, Canada's first luxury length cigarette, and St. Moritz, Canada's first luxury length menthol cigarette. During the year more than a million dollars was invested in these brands, as well as a third luxury length cigarette, Rembrandt, which was placed in distribution in mid-year.

FINANCIAL YEARS ENDED JUNE 30	1967	1966	INCREASE
SALES	\$166,014,000	\$147,076,000	13%
EARNINGS:			
Before Taxes	7,712,000	6,590,000	17%
Net	3,763,000	3,166,000	19%
Per Common Share	\$2.89	\$2.44	19%

Earnings Before Tax and Net Earnings

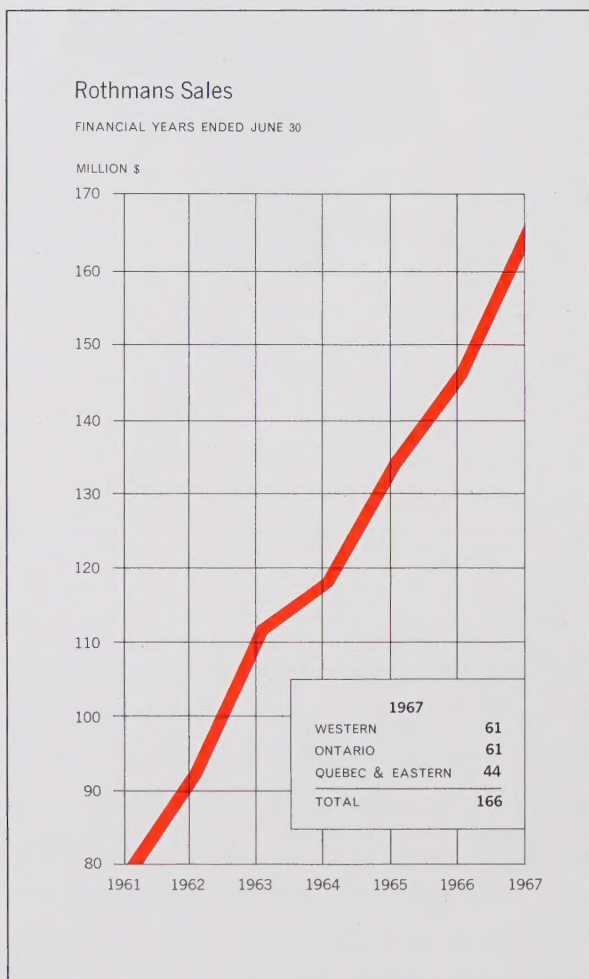
FINANCIAL YEARS ENDED JUNE 30



All three luxury length cigarettes were originally sold at a 5 cents per pack premium over the regular cigarette price until April 1967 when competition introduced a luxury length cigarette at regular price. Your Company immediately reduced the price of its luxury length cigarettes to regular price, in order to fully exploit the potential of its new "firsts."

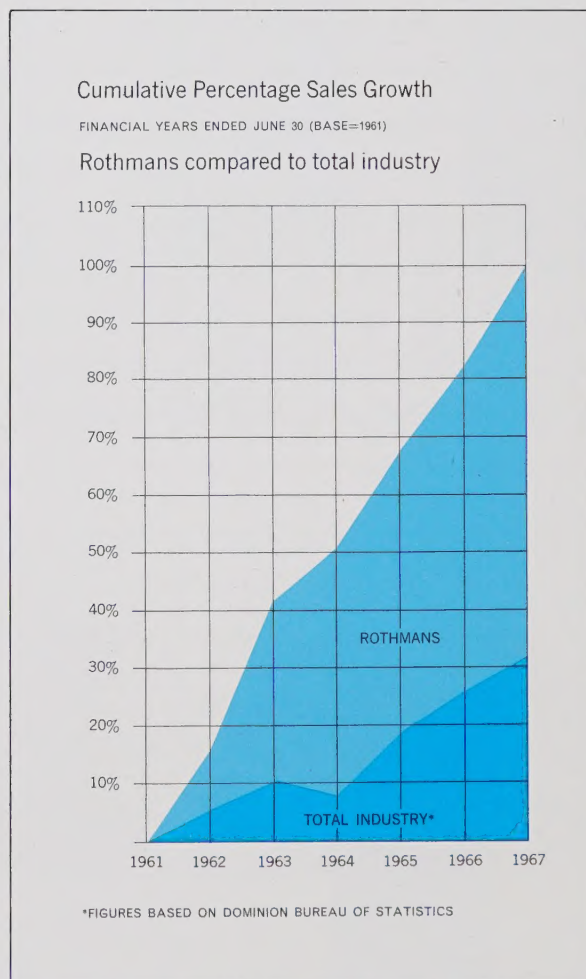
While luxury length cigarettes presently represent less than 5 percent of total market, your Company believes this market segment could have the same potential as king size products had in 1957 when Rothmans introduced Canada's first king size cigarette. In the short term, the reduced margins on luxury length brands have affected and will affect profitability; however, substantial gains can result from market penetration, as was the case with king size products.

The following graph shows the seven-year sales history of your Company, as well as a breakdown of sales for 1967:



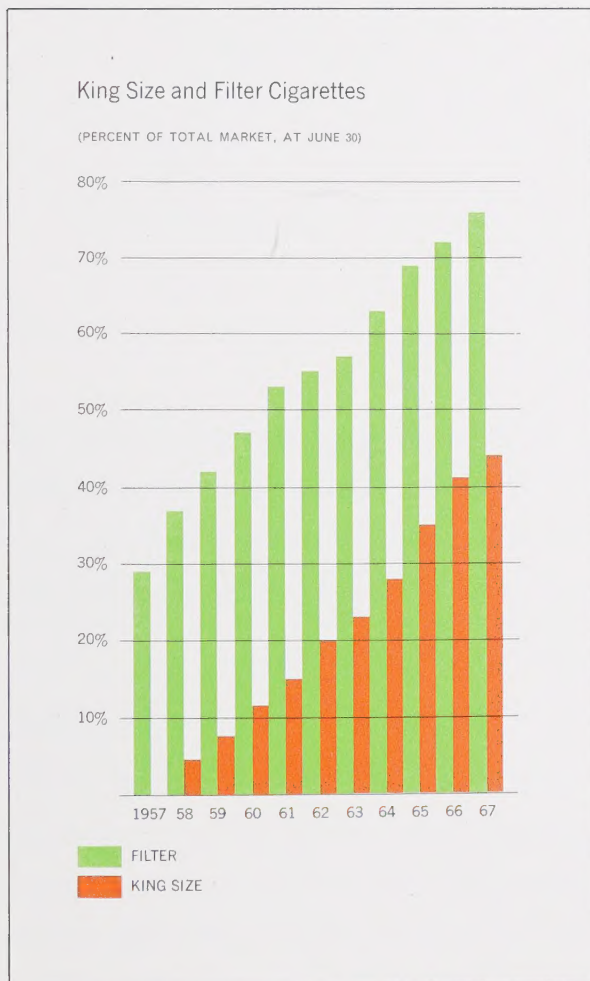
Total industry cigarette production, as reported by the Dominion Bureau of Statistics, set a new record and increased by 4.9 percent, from 45,085 million for the 12-month period ended June 1966, to 47,285 million for the same period in 1967. As mentioned in previous annual reports, industry production figures are not an accurate measure of over-the-counter sales.

The following graph compares Rothmans of Pall Mall Canada Limited sales performance with total industry over a seven-year period, using 1961 as a base:



Your Company's sales continued to outpace the growth of the total industry and increased by 914,000,000 cigarettes or 9.7 percent, from 9,474 million cigarettes in 1966 to 10,388 million cigarettes in the year under review.

Filter cigarettes, and particularly king size filter products, continue to take an increasing share of the total market. Filter cigarettes now represent 76 percent of the total market, compared to 72 percent a year ago. King size cigarettes have increased to 44 percent of total market, compared to 41 percent a year ago.



Since your Company's products are predominantly king size and filter, the Company continues to outperform the total industry. Rothmans King Size continued to be Canada's largest selling king size brand, and increased sales by more than 11 percent during the year.

Coupon and "give-away" or promotion brands continued to increase share of market and now have 19 percent of total market, versus 17 percent a year ago. Your Company's Number 7 cigarette continues to be a strong contender in this market segment, and is showing good growth.

While menthol cigarettes continue to increase, their share of market remains relatively static at 6 percent. Craven Menthol is the fastest growing menthol brand in Canada, and its sales growth last year of 39.7 percent has firmly established it as the second largest selling menthol brand in Canada. St. Moritz has been well received and shows substantial increases each month.

Craven King Size, in its first full year of national distribution, was well received and together with Craven "A" showed a sales increase of more than 10 percent during the year.

A new concept in the organization of the Marketing Division was instituted in April. This is more fully described on page 21.

During the year there were two cigarette price increases; the first effective August 1966, and the other in February 1967. Each raised the retail

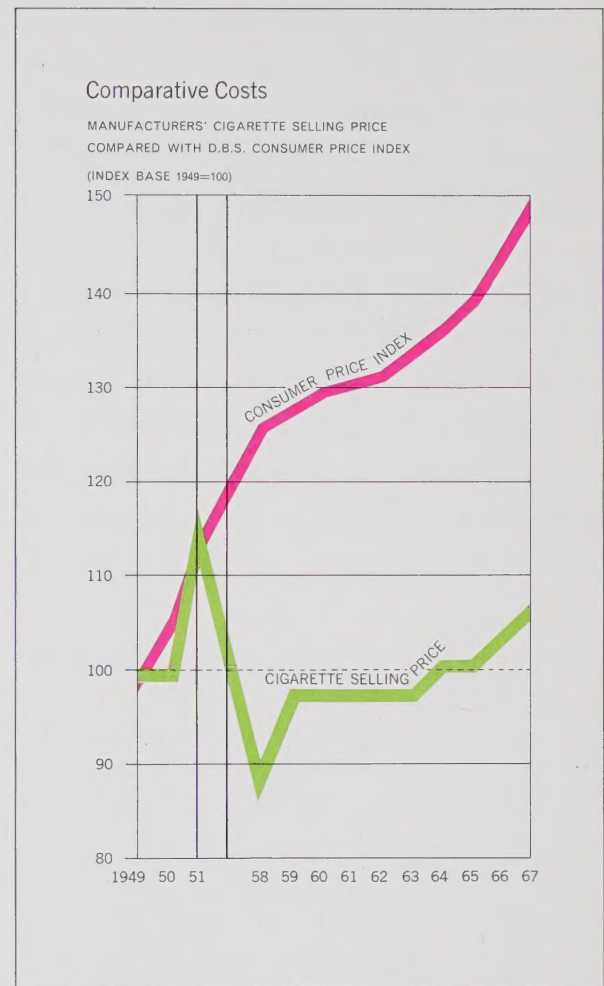
price of cigarettes by one cent per pack. As is explained in more detail in the financial section of this report, the gains from the higher cigarette prices were almost entirely offset by increased costs.

The manufacturers' selling price of cigarettes is currently 8 percent higher than in 1949. This compares with an increase in the consumer price index, as compiled by the Dominion Bureau of Statistics, of 49 percent over the same period.

The Canadian tobacco industry is presently paying close to \$500 million per year to the Federal Treasury in the form of tobacco and sales taxes. In addition, the Provincial governments receive approximately \$80 million per year from cigarettes and other tobacco products in Provincial sales taxes.

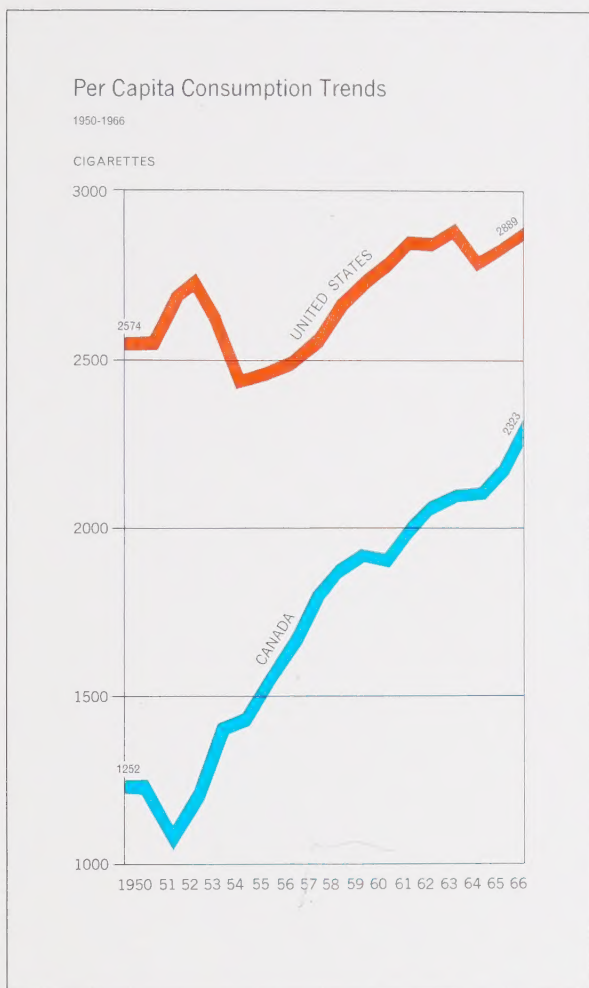
The 1966 Ontario flue-cured tobacco crop reached a record price of 71.4 cents per pound, compared to 66 cents for the 1965 crop. This year 138,709 acres have been allotted for tobacco growing, compared to 117,548 in 1966. Despite the substantial increase in acreage, it is presently estimated that the crop will yield approximately 220 million pounds, compared to 215 million pounds last year. Because of the world shortage of tobacco, your Company does not anticipate any significant change in the price of the current crop as compared to the 1966 crop.

High tobacco costs, as well as inflationary pressures, created substantial cost increases during the



year. As stated earlier, these were basically offset by price increases; however, production efficiencies, through reduced waste and more production manpower utilization, also showed continued improvement.

The Toronto factory is entirely equipped with the most advanced cigarette production machinery in the world, and the Quebec factory is in the process of being converted to the same equipment as efficiently as it can be accomplished in a multi-brand factory.



The Toronto manufacturing complex is presently housed in three leased buildings. The Company has options to purchase two of the buildings at a total cost of \$750,000. The purchase option on the one building expires in December 1967, and the other in January 1968. The lease for the third building, which is the extension completed in 1966, does not provide for a purchase option.

The Company has indicated to the owners of the first two buildings its intention to exercise these options, and provision has been made in the capital expenditure appropriation for this purchase.

Since the possibility of additional expansion in the Toronto complex is limited, the Company has agreed to purchase 35 acres of land at the corner of Dufferin Street and Steeles Avenue in suburban Toronto. This land is four miles from the present factory and, therefore, is sufficiently close to utilize present labour skills. The vendor has the right to re-purchase the land from Rothmans should the Company decide not to build on this land within a four-year period. The Company is now assured of access to suitable land in the next few years while new developments in the market and production equipment are being studied.

In Quebec, a new warehouse will be completed this fall for the storage of raw materials and finished goods. This will greatly expand the productive area of the existing factory.

The Shareholders' Annual Meeting will take place on Thursday, October 5, 1967, at which time a statement will be made regarding dividends. The formal notice of meeting, information circular and proxy form are sent with this report.

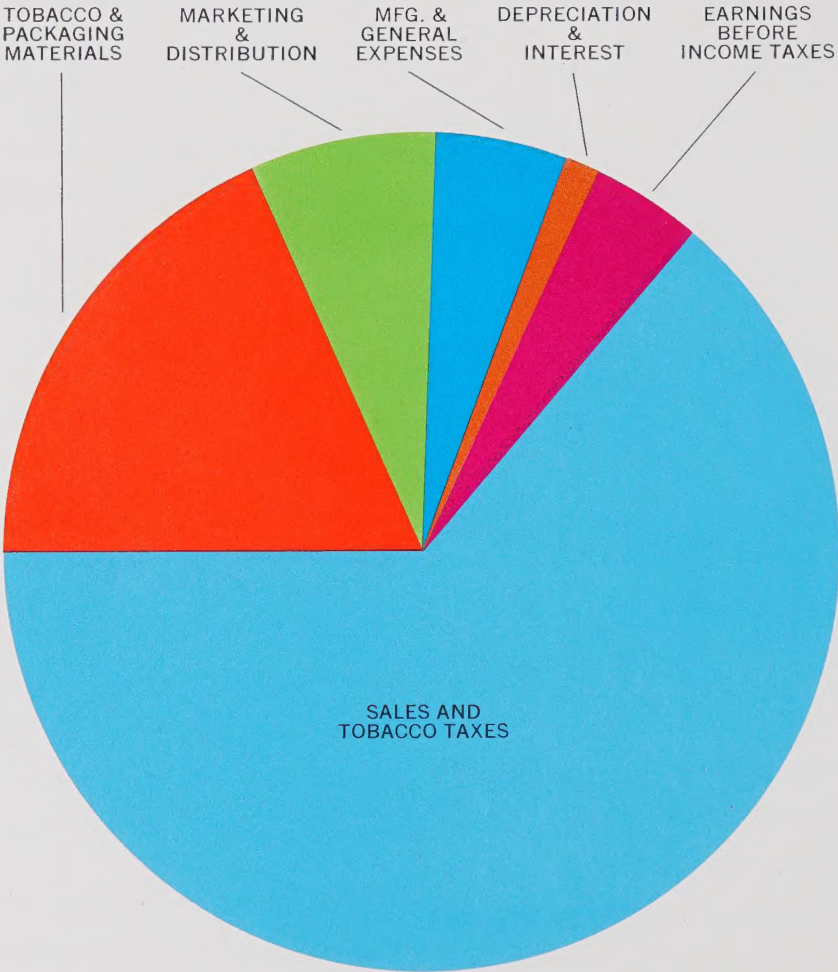
On behalf of the Board of Directors, I would like to thank all of the employees of Rothmans for their dedication, loyalty and excellent co-operation during the past year.

John H. Devlin

President

Distribution of Sales Dollar

AS A PERCENT OF TOTAL SALES



FINANCIAL YEARS
ENDED JUNE 30

1967 63.6%

1966 65.1%



18.3%

17.6%



6.6%

6.3%



5.1%

4.8%



1.8%

1.7%



4.6%

4.5%

Six-Year Financial Review

(in thousands of dollars)

Financial Years Ended June 30:

<i>Sales</i>	<i>1967</i>	<i>1966</i>	<i>1965</i>	<i>1964</i>	<i>1963</i>	<i>1962</i>
Cigarettes - - - - -	\$161,887	\$142,689	\$130,007	\$115,051	\$108,376	\$88,291
Other tobacco products - - - - -	4,127	4,387	4,797	4,013	3,877	3,910
Net sales - - - - -	166,014	147,076	134,804	119,064	112,253	92,201
Sales and tobacco taxes - - - - -	105,609	95,791	88,116	79,356	74,742	61,770
Sales, excluding sales and tobacco taxes - - - -	60,405	51,285	46,688	39,708	37,511	30,431
<i>Earnings</i>						
Earnings—before income taxes - - - - -	7,712	6,590	5,297	2,308	1,632	2,493
Income taxes - - - - -	3,949	3,424	2,839	1,302	821	12
Net earnings - - - - -	3,763	3,166	2,458	1,006	811	2,505
—as a percent of net sales - - - - -	2.3%	2.2%	1.8%	0.8%	0.7%	2.7%
—as a percent of sales exclusive of sales and tobacco taxes - - - - -	6.2%	6.2%	5.3%	2.5%	2.2%	8.2%
Net earnings per common share - - - - -	\$2.89	\$2.44	\$1.89	\$0.77	\$0.62	\$1.93
<i>Capital Expenditure—Net</i>						
Machinery and equipment - - - - -	1,704	1,077	1,716	1,523	109	178
Other fixed assets - - - - -	306	1,065	344	295	297	207
	2,010	2,142	2,060	1,818	406	385
<i>Depreciation</i> - - - - -	1,504	1,376	1,226	1,162	1,001	1,025
<i>Working Capital</i>						
Current assets - - - - -	57,465	43,744	38,431	32,068	29,945	26,519
Current liabilities - - - - -	45,194	34,042	32,439	25,772	22,277	19,786
Balance June 30th - - - - -	12,271	9,702	5,992	6,296	7,668	6,733
Working capital ratio - - - - -	1.27	1.28	1.18	1.24	1.34	1.34
<i>Indebtedness and Interest</i>						
Long-term debt - - - - -	301	301	301	3,424	6,490	7,675
Bank loans - - - - -	32,699	25,281	20,358	16,499	15,396	12,831
Interest paid - - - - -	1,413	1,145	1,133	1,045	804	638
<i>Total Assets</i>						
Current assets - - - - -	57,465	43,744	38,431	32,068	29,945	26,519
Fixed assets—net - - - - -	8,061	7,555	6,789	5,955	5,266	5,801
Other assets - - - - -	227	44	—	—	172	241
Intangible assets - - - - -	3,467	3,452	8,835	10,030	11,235	12,700
Total assets - - - - -	69,220	54,795	54,055	48,053	46,618	45,261
<i>Common Shareholders' Equity</i>						
Common share capital issued - - - - -	13,000	13,000	13,000	13,000	13,000	13,000
Common shareholders' tangible equity - - - - -	18,419	15,571	12,480	8,827	6,616	5,100
Tangible equity per common share - - - - -	\$14.17	\$11.98	\$9.60	\$6.79	\$5.09	\$3.92

Consolidated Balance

ASSETS

	1967	1966
Current Assets:		
<i>Accounts receivable—</i>		
Trade - - - - -	\$ 7,534,000	\$ 6,484,000
Affiliated companies - - - - -	139,000	27,000
Other - - - - -	361,000	162,000
	<u>8,034,000</u>	<u>6,673,000</u>
<i>Inventories, at average cost—</i>		
Leaf tobacco - - - - -	33,480,000	24,675,000
Manufactured stock - - - - -	13,245,000	10,757,000
Packaging material and other - - - - -	2,218,000	1,415,000
	<u>48,943,000</u>	<u>36,847,000</u>
<i>Prepaid expenses - - - - -</i>	488,000	224,000
Total Current Assets - - - - -	<u>57,465,000</u>	<u>43,744,000</u>
Refundable Tax - - - - -	227,000	44,000
Fixed Assets, at cost (Note 1) - - - - -	17,670,000	16,274,000
<i>Less—Accumulated depreciation - - - - -</i>	9,609,000	8,719,000
Total Fixed Assets - - - - -	<u>8,061,000</u>	<u>7,555,000</u>
Intangible Assets:		
Goodwill, at cost (Note 2) - - - - -	3,338,000	3,338,000
Trademarks, at cost - - - - -	129,000	114,000
Total Intangible Assets - - - - -	<u>3,467,000</u>	<u>3,452,000</u>
APPROVED ON BEHALF OF THE BOARD:		
JOHN H. DEVLIN, <i>Director</i>		
JOEL W. ALDRED, <i>Director</i>		
	<u>\$69,220,000</u>	<u>\$54,795,000</u>

NOTES TO FINANCIAL STATEMENTS (*Continued*)

4. Class “A” and Class “B” Shares:

The Class “A” Redeemable Deferred shares, non-dividend bearing, and non-voting (except in circumstances defined by By-law No. 12), will be redeemable only to the extent of available funds. As more fully set out in By-law No. 12, available funds means consolidated earnings in excess of \$780,000 per annum (equivalent to 6% of the company’s \$13,000,000 invested capital) computed on a cumulative basis commencing with the year ending June 30, 1966. Redemption of the shares is to be made at the rate of \$10,000 per share commencing December 31, 1966 up to a maximum of 90 shares per annum. Consolidated earnings for the year ended June 30, 1966 exceeded the requirements for available funds. 90 Class “A” Redeemable Deferred shares with a total par value of \$900,000 were therefore redeemed at December 31, 1966 and the remaining 90 shares will be redeemed by December 31, 1967.

The Class “B” Convertible Deferred shares, non-dividend bearing, and non-voting (except in circumstances defined by By-law No. 12), will be convertible at one time, but not from time to time, upon the basis of one Class “B” share for one common share. These shares will only be eligible for conversion to the extent of designated funds. As more fully set out in By-law No. 12, designated funds means consolidated earnings in excess of \$780,000 per annum (equivalent to 6% of the company’s \$13,000,000 invested capital) computed on a cumulative basis commencing with the fiscal year in which the balance of Class “A” shares have been redeemed. (Inasmuch as all the Class “A” shares will be redeemed by December 31, 1967 the accumulation of designated funds commenced on July 1, 1967.) When designated funds reach \$3,000,000, the whole of the issue will be converted. In the event that such designated funds do not reach \$3,000,000 by the end of the year ending June 30, 1975, shares equivalent to the amount of the designated funds at that date will be converted on the basis of one share for each \$10 of designated funds, and the balance of the Class “B” shares will be surrendered to Rothmans of Pall Mall Canada Limited for cancellation. In the event that there are no such designated funds by June 30, 1975, all of the Class “B” Convertible Deferred shares will be surrendered to Rothmans of Pall Mall Canada Limited for cancellation.

5. Retained Earnings:

Retained earnings includes \$900,000 which was designated as capital surplus on the redemption of 90 Class “A” shares at December 31, 1966. An additional \$900,000 will be designated as capital surplus on redemption of the remaining 90 Class “A” shares by December 31, 1967.

6. Remuneration of Directors:

Total remuneration paid to directors during the year ended June 30, 1967, in their capacity as directors or officers, amounted to \$214,000 (1966—\$138,000).

Consolidated Balance Sheet—June 30, 1967

	1967	1966
- - -	\$ 7,534,000	\$ 6,484,000
- - -	139,000	27,000
- - -	361,000	162,000
	<u>8,034,000</u>	<u>6,673,000</u>
- - -	33,480,000	24,675,000
- - -	13,245,000	10,757,000
- - -	2,218,000	1,415,000
	<u>48,943,000</u>	<u>36,847,000</u>
- - -	488,000	224,000
- - -	<u>57,465,000</u>	<u>43,744,000</u>
- - -	227,000	44,000
- - -	17,670,000	16,274,000
- - -	9,609,000	8,719,000
- - -	<u>8,061,000</u>	<u>7,555,000</u>
- - -	3,338,000	3,338,000
- - -	129,000	114,000
- - -	<u>3,467,000</u>	<u>3,452,000</u>
	<u>\$69,220,000</u>	<u>\$54,795,000</u>

ABILITIES AND SHAREHOLDERS' EQUITY

	<u>1967</u>	<u>1966</u>
Current Liabilities:		
Bank loan (secured by inventories and accounts receivable) - - - -	\$32,699,000	\$25,281,000
Accounts payable and accrued - - - - - - - - - -	2,834,000	2,024,000
Income taxes - - - - - - - - - -	3,542,000	1,063,000
Excise, sales and other taxes - - - - - - - - - -	6,119,000	5,674,000
Total Current Liabilities - - - - - - - - - -	<u>45,194,000</u>	<u>34,042,000</u>
Deferred Income Taxes (Note 3) - - - - - - - - - -	939,000	529,000
Provision for Retirement Annuities - - - - - - - - - -	<u>301,000</u>	<u>301,000</u>
Total Liabilities - - - - - - - - - -	<u>46,434,000</u>	<u>34,872,000</u>

Shareholders' Equity:

Capital stock (Note 4)—		
Authorized—		
1,600,000 common shares without nominal or par value		
180 Class “A” Redeemable Deferred shares of a par value of \$10,000 each		
300,000 Class “B” Convertible Deferred shares without nominal or par value		
Issued—		
1,300,000 common shares - - - - -	13,000,000	13,000,000
90 Class “A” shares (90 shares redeemed for cash on December 31, 1966) - - - - -	900,000	1,800,000
300,000 Class “B” shares - - - - -	3,000,000	3,000,000
	16,900,000	17,800,000
Retained earnings (Note 5) - - - - -	5,886,000	2,123,000
Total Shareholders’ Equity - - - - -	22,786,000	19,923,000
	<u>\$69,220,000</u>	<u>\$54,795,000</u>

Notes to Financial Statements

JUNE 30, 1967

1. Fixed Assets and Depreciation:

		1967		1966	
		Assets	Accumulated depreciation	Assets	Accumulated depreciation
Land	- - - - -	\$ 209,000	—	\$ 209,000	—
Buildings	- - - - -	2,786,000	1,329,000	2,779,000	1,222,000
Machinery	- - - - -	12,765,000	7,642,000	11,431,000	6,994,000
Motor vehicles	- - - - -	624,000	311,000	539,000	265,000
Leasehold improvements	- - - - -	1,286,000	327,000	1,316,000	238,000
		\$17,670,000	9,609,000	\$16,274,000	8,719,000

Depreciation has been recorded using generally the diminishing balance method at the rates normally allowed for federal tax purposes. Depreciation charged to operations during the year also includes an amount of \$112,000 based on the volume of production (1966—\$105,000).

Capital expenditures for the year ending June 30, 1968 are expected to aggregate \$5,000,000, which includes \$2,050,000 relative to purchases of land and buildings. At June 30, 1967, \$3,250,000 of this expenditure had been committed.

Rentals payable under lease agreements approximate \$280,000 annually. Of this amount \$190,000 is committed for a term of not more than four years and the remainder for an average term of ten years.

2. Goodwill:

The goodwill of \$3,338,000 arose from the acquisition of the total capital stock of Rock City Tobacco Company (1960) Limited. The Class "B" Convertible Deferred shares represent \$3,000,000 of this amount.

3. Deferred Income Taxes:

Since the company can claim more depreciation for tax purposes than was recorded in the accounts, estimated income taxes payable in 1967 are less than the amount charged against earnings. This reduction, amounting to \$410,000, has been included in the total of \$939,000 set aside on the balance sheet as deferred income taxes.

ROTHMANS OF PALL MALL CANADA LIMITED

(incorporated under the Canada Corporations Act on May 8, 1956)

AND SUBSIDIARY COMPANIES

Consolidated Statement of Earnings

FOR THE YEAR ENDED JUNE 30, 1967

	1967	1966
Sales - - - - -	\$166,014,000	\$147,076,000
Costs:		
Sales and tobacco taxes - - - - -	105,609,000	95,791,000
Tobacco and packaging materials - - - - -	30,372,000	25,877,000
Manufacturing and general expenses - - - - -	8,450,000	7,129,000
Marketing and distribution - - - - -	10,954,000	9,168,000
Depreciation (Note 1) - - - - -	1,504,000	1,376,000
Interest - - - - -	1,413,000	1,145,000
	<u>158,302,000</u>	<u>140,486,000</u>
Earnings for the year before income taxes - - - - -	7,712,000	6,590,000
Income taxes (Note 3) - - - - -	3,949,000	3,424,000
Earnings for the year - - - - -	<u>\$ 3,763,000</u>	<u>\$ 3,166,000</u>

Consolidated Statement of Retained Earnings

FOR THE YEAR ENDED JUNE 30, 1967

	1967	1966
Balance at beginning of year - - - - -	\$ 2,123,000	\$ 3,515,000
Earnings for the year - - - - -	3,763,000	3,166,000
	<u>5,886,000</u>	<u>6,681,000</u>
Amortization of establishment account - - - - -	—	4,558,000
Balance at end of year - - - - -	<u>\$ 5,886,000</u>	<u>\$ 2,123,000</u>

ROTHMANS OF PALL MALL CANADA LIMITED

(incorporated under the Canada Corporations Act on May 8, 1956)

AND SUBSIDIARY COMPANIES

Consolidated Statement of Changes in Working Capital

FOR THE YEAR ENDED JUNE 30, 1967

<i>Working capital was increased by:</i>	<u>1967</u>	<u>1966</u>
Earnings for the year - - - - -	\$ 3,763,000	\$ 3,166,000
Add—Expenses not involving a current outlay of funds—		
Depreciation - - - - -	1,504,000	1,376,000
Deferred income taxes (Note 3) - - - - -	410,000	1,354,000
Funds from operations - - - - -	<u>5,677,000</u>	<u>5,896,000</u>
<i>Working capital was decreased by:</i>		
Fixed asset acquisitions—net - - - - -	2,010,000	2,142,000
Refundable tax - - - - -	183,000	44,000
Redemption of 90 Class “A” shares - - - - -	900,000	—
Trademarks - - - - -	15,000	—
	<u>3,108,000</u>	<u>2,186,000</u>
Increase in working capital - - - - -	2,569,000	3,710,000
Working capital, beginning of year - - - - -	9,702,000	5,992,000
Working capital, end of year - - - - -	<u>\$12,271,000</u>	<u>\$ 9,702,000</u>
Current assets - - - - -	\$57,465,000	\$43,744,000
Current liabilities - - - - -	45,194,000	34,042,000
Working capital - - - - -	<u>\$12,271,000</u>	<u>\$ 9,702,000</u>

AUDITORS' REPORT

TO THE SHAREHOLDERS OF ROTHMANS OF PALL MALL CANADA LIMITED:

We have examined the consolidated balance sheet of Rothmans of Pall Mall Canada Limited and subsidiary companies as at June 30, 1967 and the consolidated statements of earnings, retained earnings and changes in working capital for the year then ended. Our examination included a general review of the accounting procedures and such tests of the accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion the financial statements on pages 10 through 15 present fairly the financial position of the companies as at June 30, 1967 and the results of their operations and the changes in working capital for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

TORONTO, July 28, 1967.

PRICE WATERHOUSE & CO., Chartered Accountants.

Financial

EARNINGS

The increase in earnings in 1967 over the 1966 financial year was attributable mainly to higher cigarette sales and two cigarette price increases. Expressed as a percentage of sales, earnings before tax increased from 4.5 percent to 4.7 percent while net earnings rose by .1 percent from 2.2 percent in 1966 to 2.3 percent in 1967.

The manufacturers' selling price of cigarettes was increased in August 1966 and again in February 1967. In each instance the retail price of cigarettes increased by one cent per pack.

The revenue realized from the higher cigarette prices was almost entirely offset by increased costs, particularly tobacco.

Costs and Earnings (per pound of tobacco used)

<i>Financial years ended June 30:</i>	<u>1967</u>	<u>1966</u>
Tobacco used in sales (millions of pounds)	25.6	23.6

Per pound of tobacco:

Sales and tobacco taxes.....	\$4.12	\$4.05
Leaf tobacco.....	.81	.74
Packaging materials.....	.37	.35
Manufacturing and general expenses....	.33	.30
Marketing and distribution.....	.43	.39
Depreciation and interest.....	.12	.11
Total costs.....	<u>6.18</u>	<u>5.94</u>
Earnings before tax.....	.30	.28
Net sales value.....	<u>\$6.48</u>	<u>\$6.22</u>

COSTS

Sales and Tobacco Taxes

Federal sales taxes were higher due to an increase of the rate from 11 percent to 12 percent effective January 1, 1967, as well as the higher sales taxes based on the increased cigarette prices.

There were no changes in tobacco taxes and duties during the year. The cost to the Company per unit of sale was lower due to the increase in export sales, since no sales or tobacco taxes are levied on cigarettes exported.

Tobacco and Packaging Materials

<i>Ontario Tobacco Crop</i>	<u>1966/67</u>	<u>1965/66</u>
Average price paid by the industry.....	71.4¢	66.0¢
Average price paid by Rothmans.....	75.0¢	67.2¢

During the year under review, the average cost of tobacco used amounted to 81 cents per pound compared to 74 cents in 1966. This increase reflected the continuous rise in tobacco prices since 1963.

Inventories of tobacco at June 30, 1967, were 39,700,000 pounds valued at 84.3 cents per pound (1966: 31,700,000 pounds—77.7 cents per pound). Tobacco inventories are valued at an average of the cost of existing inventories and new crop purchases. The purchases are taken into account at the end of February or March of each year depending on when the tobacco auctions close. The value of inventories includes the initial purchase price and processing costs.

Packaging material cost per unit of sale increased by nearly 6 percent compared with 1966. The cost of all elements of packaging materials including board, printing, foil and cellophane increased during the year.

Costs were considerably higher for luxury length cigarettes. These cigarettes, being longer, require more tobacco and packaging materials. In addition, the tobacco blends and high quality packaging for luxury length cigarettes are much more expensive than for other brands.

Marketing and Distribution

Marketing and distribution expenses increased from \$9,168,000 in 1966 to \$10,954,000 — an increase of 19.5 percent.

Advertising media rates overall increased by approximately 5 percent. In addition, advertising expenditure for the development of the Company's luxury length brands was in excess of \$1,250,000.

Distribution costs were higher as a result of rate increases by freight carriers in 1966.

Manufacturing and General Expenses

Manufacturing and general expenses increased by 18.5 percent to \$8,450,000 in 1967 compared to \$7,129,000 for the previous year.

Manufacturing wages and salaries were higher. In the case of hourly-paid employees, the Company granted bonuses in addition to increased wage rates provided for in the labour contracts. The three-year labour contracts entered into by the Company in 1964 and 1965 in Toronto and Quebec provided for a 10 cent per hour wage increase in the first year and 8 cents for each of the next two years. These contracts come up for renewal in November 1967 and March 1968 in the Toronto and Quebec factories, respectively.

This was the first complete year of operation in the extended Toronto factory. As a result, manufacturing overheads for the new addition were absorbed for the entire year under review, while in the previous financial year these expenses were in effect for only part of the period.



Depreciation and Interest

Depreciation for the year under review amounted to \$1,504,000, representing 18.7 percent of net fixed asset value at year end (1966: \$1,376,000—18.2 percent).

Interest paid during the year compared to the year previous was as follows:

<i>Financial years ended June 30:</i>	1967	1966
Bank.....	\$1,413,000	\$1,056,000
Notes payable.....	—	77,000
Other.....	—	12,000
	<u>\$1,413,000</u>	<u>\$1,145,000</u>

Interest payments increased due to higher interest rates and larger bank loans. The loans increased as a result of higher inventories attributable to increased volume. Because cigarette manufacturers require a tobacco inventory duration in excess of one year, leaf inventories increase at a faster rate than sales in time of rising volume. In addition, the value of leaf inventories was also larger as a result of higher tobacco prices. Inventories of the finished product were also higher due to increased volume, unit cost and the introduction of additional brands.

Income Taxes

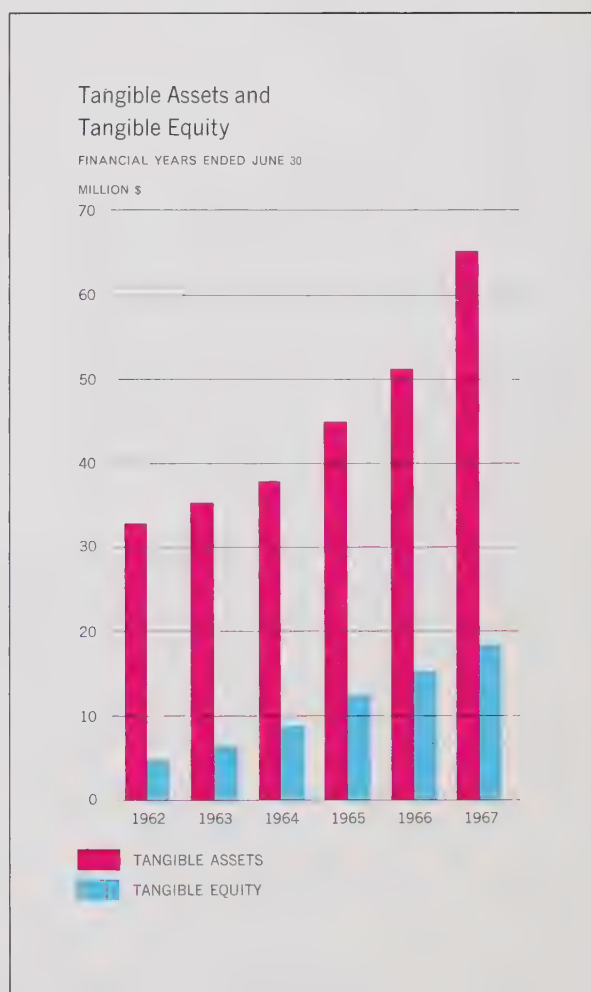
Income taxes payable for the year under review amounted to \$3,539,000 (1966: \$2,070,000) compared to \$3,949,000 (1966: \$3,424,000) charged against earnings. The difference, which arose from the ability of the Company to claim a larger amount in depreciation for tax purposes than was charged in the books of account, was credited to deferred income taxes.

FINANCIAL POSITION

The financial position strengthened in terms of substantial improvements in the Company's shareholders' tangible equity and working capital position.

Shareholders' Equity

During the year under review, the Common Shareholders' Equity increased by \$2,848,000 to \$18,419,000, or from \$11.98 per Common share to \$14.17 per Common share.



Of the 180 Class “A” shares, 90 were redeemed on December 31, 1966 at a value of \$900,000. The remaining 90 Class “A” shares are now eligible for redemption and these will be redeemed, also at a value of \$900,000, not later than December 31, 1967.

The earliest possible date for the conversion of the 300,000 Class “B” shares into Common shares is June 30, 1968.

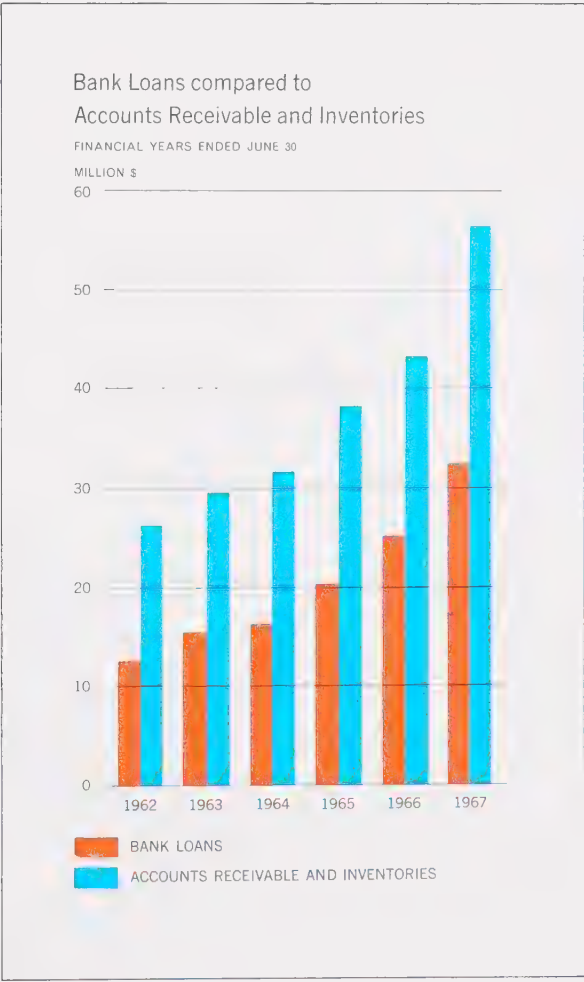
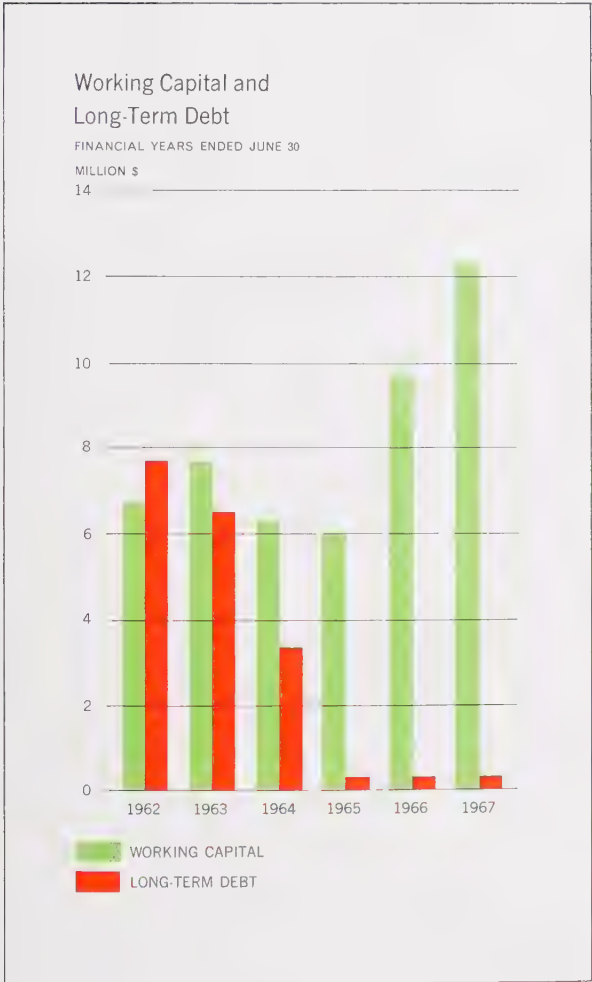
The conditions for redemption and conversion of the Class “A” and Class “B” shares, respectively, are set out in Note 4 to the financial statements.

Working Capital

Working capital at June 30, 1967, amounted to \$12,271,000, compared to \$9,702,000 in 1966, an increase of \$2,569,000. The detailed Statement of Changes in Working Capital is presented on page 15 of this report.

Bank Loans

Bank loans at June 30, 1967, were \$32,699,000 compared to \$25,281,000 in 1966. The increase in bank loans is attributable to higher inventories and accounts receivable as outlined earlier in this report.



The following analysis outlines the changes in bank loans over the past two financial years:

(\$000)	1967	1966
<i>Bank loans were increased by:</i>		
Current assets—increase		
Inventories	12,096	4,419
Accounts receivable and other	1,625	894
	<u>13,721</u>	<u>5,313</u>
<i>Bank loans were reduced by:</i>		
Other current liabilities		
—increase (decrease)	3,734	(3,320)
Increase in working capital	2,569	3,710
	<u>6,303</u>	<u>390</u>
Net change in bank loans	7,418	4,923
<i>Bank loans:</i>		
Beginning of year	25,281	20,358
End of year	<u>32,699</u>	<u>25,281</u>

Capital Expenditure

Net capital expenditure for the year amounted to \$2,010,000 (1966: \$2,142,000). Of this amount, \$1,706,000 was utilized for machinery and equipment in the Quebec and Toronto factories.

Capital expenditure for the year ended June 30, 1968 is budgeted at \$5,000,000. This includes \$600,000 for equipment on which delivery was originally scheduled for the 1966/67 financial year. An amount of \$750,000 has been allocated for the possible purchase of two of the buildings in the present Toronto manufacturing complex. The 35 acres of land referred to in the Directors' Report will require a further \$800,000. A new warehouse to provide for storage of both raw materials and finished stocks will be built in Quebec at an anticipated cost of \$700,000. The

remainder of the capital expenditure budget will be utilized mainly for additional productive equipment in the Toronto and Quebec factories.



Distribution of Sales Dollar

A chart outlining the main elements of costs as a percentage of total sales is given on page 8 of this report.

Note

The Consolidated Statement of Earnings this year includes a comprehensive breakdown of the Company's costs (page 14).

MARKETING

During the year the Marketing Division of the Company was entirely reorganized into six operating regions, with General Managers in charge of each area reporting to the Vice President Marketing.

Marketing responsibilities were re-aligned to give each of the General Managers more authority over selling, advertising, public relations, promotions and budgets. As a result of this change, the marketing group at head office has been reduced to a small service staff to support the General Managers over their whole range of activities. The Company now possesses one of the most modern marketing organizations for consumer products in North America.

Brands continue to be supported in a variety of advertising media with close co-operation between the Company's advertising agency and internal creative department. In

addition to formal media advertising, a wide range of promotional activities was carried out in support of the main brands.

Your Company's contribution to the visual and performing arts in Canada has been widely recognized. A contribution to the restoration of two public utilities buildings (circa 1883) in the City of Stratford resulted in the Rothmans Art Gallery of Stratford becoming established as one of the leading smaller galleries in the country. Under the direction of the Stratford Art Association, it is becoming well known and highly regarded.

Other contributions included the sponsorship of Centennial Sculpture '67 in Vancouver, the presentation of a collection of contemporary French tapestry in some provinces, the provision of souvenir programs, carrying exclusive Rothmans King Size advertising, for the



Rothmans Art Gallery of Stratford



Centennial Sculpture '67 Vancouver

Contemporary French Tapestry Exhibit



Dominion Drama Festival, National Ballet, Comédie-Canadienne, Les Grands Ballets Canadiens, the Shaw Festival, and many other groups.

In the course of the coming year it is planned to present the now-famous European collection of paintings, "Art in Industry," sponsored by the Peter Stuyvesant Foundation, in leading galleries across Canada, as well as a collection of fine works by contemporary Italian sculptors and painters.

Your Company contributed to the success of the Pan-American Games by providing information booths staffed by multi-lingual hostesses, and radio-controlled transportation for the benefit of the Games officials.

Rothmans Special Events Caravans continued to assist, free of charge, many non-profit organizations in their

Rothmans Information Booth, Pan-American Games



activities across Ontario and Quebec, and will soon also be doing so in other provinces. The caravans are fully equipped to function as control centres for outdoor events, and offer complete sound, lighting and communications systems. Since the inception of the Rothmans Special Events Caravans, many expressions of appreciation have been received.

Continuing a tradition of some years, Rothmans sponsored major championship equestrian and yachting events, and have given organizational and financial assistance to teams which represented Canada at the Pan-American Games in Winnipeg.

These are some examples of the wide range of cultural and national sports events in which Rothmans products are promoted effectively and with good public relations results.



Rothmans Special Events Caravan

Rothmans King Size really satisfies





ROTHMANS OF PALL MALL CANADA LIMITED

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